

January 2004

Tax law drafting: the principled method

Duncan Bentley

Bond University, Duncan_Bentley@bond.edu.au

Follow this and additional works at: <http://epublications.bond.edu.au/rlj>

Recommended Citation

Bentley, Duncan (2004) "Tax law drafting: the principled method," *Revenue Law Journal*: Vol. 14 : Iss. 1 , Article 1.
Available at: <http://epublications.bond.edu.au/rlj/vol14/iss1/1>

This Editorial is brought to you by the Faculty of Law at ePublications@bond. It has been accepted for inclusion in Revenue Law Journal by an authorized administrator of ePublications@bond. For more information, please contact [Bond University's Repository Coordinator](#).

Tax law drafting: the principled method

EDITORIAL

TAX LAW DRAFTING: THE PRINCIPLED METHOD

From 1 July 2002, the tax legislation function was moved from the Australian Taxation Office (ATO) to the Department of the Treasury (Treasury). Part of the rationale was that, as the Treasury was responsible for formulating tax policy, it should have more input into the translation of that policy into legislative design. Bringing policy and legislative development together aimed to produce a strategic alignment between Government policy and its implementation in legislation.

In March 2004, the Treasury issued its open *Review of Aspects of Income Tax Self-Assessment*. It became clear in this discussion paper and in a subsequent speech by the then Minister for Revenue and Assistant Treasurer, Senator Helen Coonan, to the Australian Institute of Company Directors in Perth on 12 July 2004, that the Government was moving towards a principle-based approach to drafting of tax legislation. The words that accompany the introduction of new drafting methods always lift the spirits of the weary tax specialist. It is tempting to reach immediately for the Hallelujah Chorus as words such as 'simple', 'flexible', 'coherent', 'efficient' and 'plain English' fall lightly from the pens of those who design and write the law.

Confusion over the numbering in the amendments to the 1936 Income Tax Assessment Act (1936 Act) was reaching high farce well before the laborious processes leading to the introduction of the *1997 Income Tax Assessment Act* (1997 Act). We are now so used to this schizophrenic legislation that we can affect surprise when a visitor from another country looks askance, as we attempt to present the two acts as one coherent whole.

So, what do we know of principle-based drafting? At a recent workshop of the Law Council of Australia Tax Subcommittee, Brenda Berkeley, Manager in the Tax Code unit of the Department of Treasury, made the following useful explanatory comments on the coherent principles approach to tax design:

- The coherent principles approach aims to write tax law in a series of operative rules, that are principled statements about what the law is intended to do, rather than details about the mechanism that gets it there.

- *Coherence* in this context means that the principle:
 - Helps the reader make sense and order out of the law;
 - Captures the essence of the intent of the law – so that it is clear on first approach;
 - Is drafted in a plain, non-technical style, avoiding the use of expressions that can only be understood by referring to definitions or other lower level rules; and
 - Is intuitive or obvious to someone who understands its intent and context.
- But, unlike some general principles approaches, the coherent principles approach can accommodate detailed or specific rules, when needed, by incorporating a plan for unfolding the principles and providing details of their application in particular cases.
 - At times that additional detail will appear in the law itself.
 - But at other times it will appear in the Explanatory Memorandum or in subordinate legislation (including regulations).
 - As at present, if experience with the law once it is enacted suggests that an ATO Ruling may be needed, the principled framework in the law will provide a sounder basis for the ruling than does the present black letter detail approach.

The benefits that Ms Berkeley put forward for the coherent principles approach were that the law will be simpler and shorter, more flexible, more stable, more certain, and because the draft law will be conceptually simpler, it will apparently provide a better basis for consultation.

Such legislation contains operative provisions to solve the majority of cases. For the more complex issues, the principles establish the framework for the ATO and taxpayers to find the answers. This framework must be clear enough that the ATO's discretion is not open-ended. We could usefully learn from the civil law jurisdictions how to draft principles that sufficiently constrain decision makers.

Subdivision 713-C of the 1997 Act, which deals with how some unit trusts should be treated like head companies of consolidated groups, is given as an example of the new principle-based drafting. Section 713-120 sets out what the subdivision is about: the corporate unit trust or public trading trust can sometimes choose to form a

TAX LAW DRAFTING: THE PRINCIPLED METHOD

consolidated group and be treated like a company and head company of the group. The treatment affects the trust, the trustee and other entities connected with the trust (such as members of the trust and entities the trustee holds membership interests in).

Subdivision 713-C as drafted does not instill confidence. There seem to be some basic misunderstandings as to the operation of the law of trusts. Treasury ought not to set out the policy approach encapsulated in an economic impact statement in a principle and then force the law to fit. While theoretically useful to have as part of the legislation a statement by Treasury of the purpose underlying the policy initiative behind the legislation, it is still policy and not law.

Legal drafting is more complex. It requires phrasing where each word will be interpreted extensively as to its particular and general meaning and specifically in the context of the sentence, the surrounding sections, like sections throughout the Act, its meaning and legal principle, decisions of the courts, both locally and internationally, and in the surrounding materials.

To take a policy statement designed for another purpose - by its very nature, political instant and transient - and to use it to deliver law that must, by its nature, be apolitical, consistent and timeless, is to undermine the purpose of legislation. The carefully crafted translation into legislation is by no means impossible, but the product is not principle in the economic sense. It reflects only one of the existing approaches to legislation. Unless it is intended to overturn the fundamental principles of legislative drafting, the direct use of the economic principles cannot be meant.

Does the principle approach revert then to the broad statements of principle set out in earlier legislative approaches? The clear principles governing the meaning of assessable income and allowable deductions were set out in ITAA 36 in sections 25(1) and 51(1). They were fundamental to the structure and operation of the 1936 Act. Their advantage lay in their brevity and clarity. The courts, the ATO and the tax-paying community spent 60 years interpreting these principles. Yet they met all the requirements of the coherent principles approach to tax design.

The 1936 Act's subsequent development illustrates how easily this approach can be hijacked by the detail deemed necessary to explain and/or constrain the operation of the principles. The drafting of the 1997 Act sought to overcome these difficulties using a principled approach expanded to incorporate broader explanation and examples. Critics may quibble over modes of address and the detail of the legislation. However, it is carefully crafted, based on principle, in plain English. Its

shortcoming is the onerous burden on drafters of reflecting in the 1997 Act the law of the 1936 Act in all its complexity 60 years on. If the 1997 Act approach is used, it will lead to clarity and accessibility. It will not necessarily reduce volume or complexity. There is no rewrite proposed. New law will use the coherent principles approach. Without starting again, is that not what the 1997 Act has sought to do?

Perhaps there really is an intention to take much of the detail in the 1997 Act out of the Act. This reflects the approach taken in the US. There, the principles of law are set out in the *Internal Revenue Code*. The detail is set out in the Regulations. As the combination is more complex and expansive than the Australian tax law, this is unlikely to be the direction intended by the coherent principles approach.

What I hope is not meant is to create a truncated law setting out the main principles of the tax law but without the legislated detail (whether legislated directly as in the 1997 Act or delegated as in the US Regulations). To do so necessitates interpretation and explanation of the principles that should be part of the legislative documentation. If it is not legislated, the ATO would be forced to issue rulings to fill the gap. This puts the ATO in the position of effective legislator, a position neither the ATO nor the taxpayer wants the ATO to fill. If the coherent principles approach is an avenue by which the legislature abrogates its responsibility to legislate, then it cannot be supported.

Plain English drafting should be encouraged. Drafters should explore the methods of drafting available to achieve the objectives of the coherent principles approach set out above. Consider different legislative structures. But remember that legal drafting is a craft of lawyers, albeit with an awareness of context and history. Remember also that law should be legislated: that is fundamental to the principle of the separation of powers.

Duncan Bentley